Supreme Court, U.S.
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No.

In The

Supreme Court of the United States

October Term, 1996

DENNIS F. KENNEDY,

Petitioner,

vs.

UNITED STATES OF AMERICA,

Respondent.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

Whether Petitioner's constitutional rights to due process and to a fair trial were violated because the Third Circuit's interpretation of this Court's decision in *Cheek v. United States*, 498 U.S. 192 (1991), is at variance with the decisions of other circuits which find that *Cheek* imposes an affirmative duty on trial courts to instruct jurors in criminal tax evasion cases that they must acquit a defendant if they find that the defendant acted in subjective good faith, notwithstanding their finding that the defendant's actions were objectively unreasonable?

Whether Petitioner's constitutional rights were violated by the Third Circuit's affirmance of the district court's decision to deny Petitioner's motion for acquittal?

Whether Petitioner's constitutional right to an untainted grand jury process was violated by the presentation of false and misleading testimony by Internal Revenue Special Agent Jacqueline Zisterer?

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Petitioner Dennis Kennedy, prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit denying Petitioner's application for *en banc* consideration and for reconsideration and affirming the judgment of conviction entered by the trial court.

OPINIONS BELOW

The court of appeals affirmed the judgment of conviction by memorandum opinion and order entered December 4, 1996 (1a, 5a)[1] and it denied Petitioner's application for *en banc* consideration and for reconsideration by judgment order. (7a). Prior to trial Petitioner moved for dismissal of the indictment because of government misconduct occurring inside the grand jury room. United States District Court Judge Dickinson R. Debevoise reserved on the motion until after the trial. On September 8, 1994, the district court filed an opinion denying Petitioner's motion. (9a).

STATEMENT OF JURISDICTION

Petitioner was originally a defendant in a criminal action brought in the United States District Court for the District of New Jersey. The district court had subject matter jurisdiction pursuant to 18 U.S.C. § 3231. The judgment of conviction was entered against Petitioner on December 15, 1994, and was docketed on December 20, 1994, following a trial. A timely appeal was filed with the United States Court of Appeals for the Third Circuit, which had appellate jurisdiction to review the judgment of the district court pursuant to 28 U.S.C. § 1291. A memorandum opinion and judgment order affirming the judgment of conviction was entered by the Third Circuit on December 4, 1996. (1a, 5a). Applications for reconsideration and for *en banc* review were subsequently filed with the Third Circuit, which entered a judgment order denying the

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1. The notation "a" refers to the appendix annexed to this petition. The notation "DA-" refers to the appendix filed by petitioner with the United States Court of Appeals for the Third Circuit.

applications on December 30, 1996. (7a). Petitioner seeks a writ of certiorari to review the judgment of the United States Court of Appeals for the Third Circuit. This Court has jurisdiction to review the judgment below pursuant to 28 U.S.C. § 1254(1).

CONSTITUTIONAL PROVISION AND STATUTE INVOLVED

The Fifth Amendment to the United States Constitution and Petitioner's constitutional right to due process are pertinent to this case. Also applicable is the statute proscribing tax evasion, 26 U.S.C. § 7201. The applicable provisions of law are set forth in the annexed appendix. (24a).

STATEMENT OF THE CASE

On October 13, 1993, a two-count indictment was returned by a United States grand jury of the district of New Jersey, against Petitioner Dennis Kennedy alleging tax evasion for the years 1986 (Count 1) and 1987 (Count 2). (Da-14). Prior to trial, Petitioner moved for dismissal of the indictment because of government misconduct occurring inside the grand jury room. United States District Court Judge Dickinson R. Debevoise reserved on the motion until after trial. On September 8, 1994, the district court filed an opinion denying Petitioner's motion. (9a). The trial began on April 18, 1994, and ended on April 21, 1994, with the jury finding Petitioner guilty on both counts of the indictment. Petitioner was sentenced on December 12, 1994, to a term of imprisonment of 4 months on each of Counts 1 and 2, with the terms to be served concurrently. (DA-5).

A. Overview

At trial, the government sought to prove that Petitioner's 1986 tax return was false and fraudulent, as alleged in Count 1 of the indictment, because he had: (1) under-reported gross receipts received by Winslow Exxon, a gas station solely-owned by

Petitioner; (2) reported a $51,760 long-term capital gain on the sale of a 55-foot ocean yacht, when the gain should have been reported as ordinary income; (3) reported a $40,862 capital loss on the sale of a 46-foot ocean yacht, which the government contended had been used primarily for personal and recreational purposes and, therefore, ineligible for deduction as a capital loss; and (4) failed to report a long-term capital gain from the sale of real estate located in Brigantine, New Jersey. (DA-689a). With respect to Count 2 of the indictment, the government alleged that Petitioner's 1987 tax return was false and fraudulent because Petitioner had: (1) again under-reported the Winslow Exxon gas station receipts; and (2) reported a $69,422 capital loss on the sale of a 48-foot Uniflite yacht, when the asset was not entitled to capital loss treatment. (DA-689a).

Petitioner disputed all of the government's contentions. He denied that he under-reported income from his gas station and he denied any intent to erroneously report or to fail to report any of the items that were the subject of the indictment. Petitioner, who had an eighth grade education, maintained that he had given to his accountants all the information necessary to prepare his tax returns and that the accountants either failed to properly analyze the information, or to ask the questions necessary to make highly technical professional accounting judgments that were required in order to determine the tax treatment of Petitioner's assets. The accountants admitted their deficiencies at trial and the trial judge, in rendering his opinion on Petitioner's motion to dismiss the indictment, specifically noted the carelessness of Petitioner's accountants (DA-691a).

B. Tax Treatment of the Brigantine House

The government claimed that Petitioner had failed to report income from the sale of a house that he had owned in Brigantine, New Jersey. The house had been purchased for $38,000 in 1974, and had been sold on April 9, 1986 for $75,000. (DA-141). Although the government claimed that Petitioner was the sole owner of the

house, Petitioner produced evidence that he owned the house jointly with his mother, Margaret Kennedy. (DA-388). In 1982, after Petitioner's mother lived in the house for about 8 years, she became ill. She moved out of the house, which was then rented, with the rental proceeds going to her. (DA-389). The rent checks were written to Petitioner and were deposited by him in his mother's account. It was his mother who had made the mortgage payments. (DA-389). Over the eight year period during which Petitioner's mother lived in the home, a screened-in porch was added at a cost of $5,000. In addition, a two-car driveway was built, and sprinklers, central air conditioning, and a new heater, among other things, were purchased. Payments for all these things were made by Petitioner. (DA-388 to DA-389).

A deed had been prepared on February 5, 1986, by attorney Michael Diamond, transferring ownership of the property from Petitioner and his mother jointly to Petitioner alone. Diamond testified that because the transfer of the property was from a mother to a son it was tax exempt. (DA-238). Petitioner's gain on the house would have been $19,500, if no improvements had been made. Petitioner demonstrated, however, that the government failed to take into account the improvements made to the house over the twelve years that it was in Petitioner's family. If these items had been considered by the government, it would have recognized that no gain was realized from the sale. Petitioner's mother had died two days before the deed prepared by Diamond had been recorded. (DA-234).

Robert Kelly, a junior accountant employed by Moore and Fitzpatrick, the accounting firm used by Petitioner, testified that he had not asked Petitioner whether he had sold any real estate in 1986. (DA-93). He noted that he should have asked the question because taxpayers are often misinformed about whether the sale of real estate is a taxable event. (DA-93). Kelly specifically stated that taxpayers are not knowledgeable about whether gifts from parents are taxable events or whether gifts from a dead parent are taxable. (DA-94). Kelly's boss, Kenneth Moore, also acknowledged

that he had not asked Petitioner about whether he had sold the Brigantine house in 1986. (DA-122).

C. Tax Treatment of the Yacht Sales

The evidence at trial established that Petitioner was trying to get into the business of selling yachts, had purchased a marina for that purpose and formed a company called Magic Marine. Petitioner had previous experience in the yacht business. He had entered into two partnerships with Stephen Gordon in 1986 and 1987, called the Marina Project and South Florida Yacht Sales respectively. (DA-52 to DA-55). Petitioner belonged to a yacht club, entered tournaments, and brought his boat to the tournaments. It was advantageous for people engaged in the business of selling yachts to engage themselves in activities at marinas in order to generate potential business. (DA-57). Three yachts, which were the subject of the indictment, had been sold by Petitioner.

The first yacht sold by Petitioner, which was the subject of Zisterer's investigation was a 46-foot boat, called the Ocean. The boat, which Petitioner had purchased for $42,500, was sold at a loss. (DA-152). The government contended that this boat was owned by Petitioner for his personal use and therefore Petitioner was not entitled to the loss taken. As alleged evidence that the boat was used for pleasure was a notation on an insurance form, where the word "pleasure" had been checked. (DA-151). Anthony Faraco, who sold Petitioner the insurance, noted that "pleasure" is the correct characterization so long as the boat owner is not charging people to walk on the boat or to take it out sailing. (DA-154 to DA-155). The word "commercial" would be checked, Faraco noted, if the boat is a commercial fishing vessel, a tugboat, or a charter boat used by a business to collect a fee. (DA-154). Petitioner maintained that the boat was purchased for investment purposes, and that he, at times, would take people out on the yacht, in the hope of inducing sales for his business. This sales strategy in fact worked. Petitioner took one man in the club, named Lawrence Littman, out on his 46-foot yacht. (DA-211). Littman subsequently bought from Petitioner a

$450,000 55-foot Ocean yacht, which is the second yacht sold by Petitioner that is the subject of the indictment. (DA-213). In addition to purchasing the 55-foot yacht from Petitioner, Littman also sold Petitioner a 48-foot Uniflite yacht for $150,000. The Uniflite yacht is the third yacht that is the subject of the indictment.

At trial, the government claimed that Petitioner had possession of the 55-foot boat for only two months and therefore was not entitled to the long term capital gain he had taken. The government also contended that Petitioner received a commission on the boat and, therefore, any gain was to be treated as ordinary income. (DA-181 to DA-185). The government's characterization was disputed, however, by Leonard Garr, the owner of Comstock Boat Works in Brick Town, New Jersey, who stated that he had sold the yacht to Petitioner and earned a commission himself of $50,000. The terms of the transaction were set forth on forms, which specifically indicated that the yacht was being purchased by Petitioner for the purpose of reselling it. (DA-185). No commission had been paid to Petitioner. (DA-185). Petitioner maintained that irrespective of whether profit on the transaction was treated as a long term or short term gain, the end result was the same: no additional taxes were owed for the year 1986. This claim was supported by the expert testimony of accountant Robert Brennan. (*See* Exhibit DX-41, DA-1817).

The third boat sold by Petitioner was the 48-foot Uniflite that had been purchased from Lawrence Littman. This boat, the government contended, was a capital asset. Petitioner bought the boat for $150,000 and sold it for $210,000, but he had made improvements to it and had paid a commission for its sale, which resulted in a loss to Petitioner. Defense counsel, in summing up to the jury, noted that the government never analyzed any of the maintenance or repair charges and therefore could not argue beyond a reasonable doubt what, if anything, Petitioner owed as a result of the transaction.

At trial, the government presented Petitioner's accountant,

Robert Kelly, with a sheet of paper captioned "1986 Magic Marine" that contained notations allegedly written by Petitioner. (DA-72, DA-85, DA-851). The document had three entries. One entry, next to the words "46 Ocean", stated a loss of $40,862.19. (DA-72, DA-851). Another entry, following the words "55 Ocean", stated a profit of $51,760. (DA-73, DA-851). The third entry, next to the words "48 Uniflite", stated a loss of $40,682. (DA-73, DA-851). On the tax returns prepared for Petitioner, the loss for the 46-foot Ocean yacht and the 55-foot Ocean yacht correlated with the notations on the handwritten summary document. (DA-73). The loss for the 48-foot Uniflite, however, was reported on Petitioner's taxes as being higher than indicated on the summary documents. The loss reported on the tax returns, of $69,422, was attributable to additional costs picked up by the accountant, which increased the tax basis of the boat. (DA-74). These costs included amounts spent by Petitioner for storage, maintenance and cleaning. (DA-79).

Kelly acknowledged that he had been supplied with folders by Petitioner for each of the yachts, which contained detailed information about their sale, but Kelly used summary information written on the outside of the folders to characterize the gains or losses as short or long term. (DA-75). Kelly had not looked inside the folders, which contained information relevant to the tax treatment of Petitioner's assets. (DA-91 to DA-92). Kelly also acknowledged that he made an error in calculating the tax basis for the 55-foot boat. (DA-92).

Kelly had been instructed by his boss, Mr. Moore, that Petitioner had held the yachts as an investment. (DA-75). It was Moore who had 90 percent of the contact with Petitioner, and, when Kelly needed information about the Kennedys' taxes, he would first go to Moore, not the clients. (DA-86). Petitioner had not told Kelly whether to treat the profits on the boats as short term or long term capital gains, he also did not tell him whether to treat property as personal or as investment. (DA-89 to DA-90). These decisions were made by Moore. (DA-90). Kelly noted that in all his personal dealings with Petitioner, he found him to be forthcoming and had willingly provided any information requested. (DA-95).

Moore confirmed the testimony of Kelly. He acknowledged that he was the one who told Kelly to treat the yachts as investment properties and it was he who told Kelly whether to characterize the yachts as long or short-term assets. (DA-108). Moore stated specifically that Petitioner had never told him that he never used his yachts for personal use. (DA-131). Moore also stated that the folders he had been given by Petitioner for the preparation of his taxes, which had not been examined, contained information relevant to Petitioner's taxes, including sales invoices, repair bills and purchase invoices. (DA-136).

D. Treatment of the Gas Station Income

In calculating the taxes owed by Petitioner as a result of the income earned from Winslow Exxon, Petitioner's accountants added the deposits in his three business accounts to determine the gross receipts of the business. The government performed the same analysis as Petitioner's accountants, but, in calculating the gross receipts, added to the business account deposits, monies deposited into Petitioner's personal account, which allegedly belonged in the business bank accounts. Petitioner offered expert testimony that showed the flaws in the methodologies of both the government and Petitioner's accountants: neither had deducted inter-account transfers and these transfers, if not considered, would have resulted in an over-reporting of income, not an under-reporting as the government contended. Petitioner's accountant, Michael Kelly, recalculated the receipts and taxes owed, after being informed of the mistake he made in not deducting inter-account transfers, and he found that Petitioner had overpaid his taxes for the gas station. (DA-376).

REASONS FOR GRANTING THE WRIT

I. PETITIONER'S CONSTITUTIONAL RIGHTS WERE VIOLATED BY THE DISTRICT COURT'S FAILURE TO ADVISE THE JURY THAT EVEN IF IT BELIEVED THAT PETITIONER'S ACTIONS WERE OBJECTIVELY UNREASONABLE, IT STILL WAS REQUIRED TO ACQUIT HIM IF IT FOUND THAT PETITIONER HAD ACTED IN SUBJECTIVE GOOD FAITH.

In instructing the jury on the requirement of willfulness, the trial judge told the jury that if the Petitioner "had a good faith misunderstanding of the law or believed in good faith that he had done all that the law required, you may not find that he acted willfully and you must acquit him." (DA-508). The court went on to state:

> It is obviously impossible to ascertain or prove directly the operations of the defendant's mind; but a careful and intelligent consideration of the facts and the circumstances shown by the evidence in any case enables one to infer what another's intentions were in doing or not doing things. With the knowledge of definite acts, you may draw definite logical conclusions.

(DA-510).

The trial judge in issuing this instruction, failed to inform the jury that Petitioner's beliefs need not be objectively reasonable for them to be in good faith: the jury could well have concluded that Petitioner, even though he had subjective good faith in dealing with his tax liability, was nevertheless acting in an objectively unreasonable way, and therefore was guilty of the offenses charged. The failure to provide the jury with instructions differentiating objective from subjective good faith, especially given the facts of this case, is reversible error. *See, e.g., Cheek v. United States,* 498 U.S. 192 (1991). *See also United States v. Pabisz,* 936 F.2d 80 (2d Cir. 1991).

Indeed, the jury was confused over the issue of reasonableness, and after a brief period of deliberations returned with the following question: "Reasonableness — is proof on a prima facie basis sufficient, or do we need specific intent on each segment of the charge to substantiate reasonableness?" (Da-515). After reading the jurors' question to counsel, the following colloquy took place:

> Defense Counsel: Do you understand they are using reasonable to refer to reasonable doubt?
>
> The Court: *I understand it to refer to the good faith defense.*
>
> Defense Counsel: So you're just going to refer them to the charge —
>
> The Court: You might be right. It may go to the burden of proof. Maybe the best thing to do is ask them just to review the charges on burden of proof and see if that doesn't answer their questions, and if they still have difficulty, to come back. In fact, we might say that, I find the question a little bit difficult to understand. Perhaps they could refer to the charges, yes.

(DA-515-16) (emphasis supplied).

Where, as in this case, the government's evidence against Petitioner was far from substantial, and the jury expressed difficulty in assessing the reasonableness of Petitioner's actions, Petitioner was entitled to a clear jury instruction on subjective good faith.

To be guilty of tax evasion in violation of 26 U.S.C. § 7201 the government must prove that Petitioner "willfully" attempted to evade or defeat a tax. In *United States v. Murdock*, 290 U.S. 389 (1933), this Court held that a defendant is entitled to an instruction with respect to whether he acted in good faith based on his *actual belief*

(emphasis added). That is, if a defendant believes in good faith that he was not violating any of the provisions of the tax laws, he cannot be found to have acted willfully, and must therefore be acquitted of the charges. In *United States v. Cheek,* this Court held that a defendant's good faith belief need not be objectively reasonable. *Cheek v. United States,* 498 U.S. 192 (1991) ("We thus disagree with the Court of Appeals' requirement that a claimed good-faith belief must be objectively reasonable if it is to be considered as possibly negating the government's evidence purporting to show a defendant's awareness of the legal duty at issue"). Consequently, it is clear that a jury instruction advising the jury that the defendant's belief must be objectively reasonable is plain error. *See United States v. Aitken,* 755 F.2d 188, 193-94 (1st Cir. 1985) (concluding that objective reasonableness instruction in willful tax evasion case was plain error despite strong evidence against defendant). The circuit and district courts have differed, however, over whether, as Petitioner maintains, this Court's decision in *Cheek* places an affirmative duty on trial courts to instruct juries on the issue of Petitioner's subjective beliefs.

For instance, the Second Circuit in *United States v. Pabisz,* 936 F.2d 80, 83 (2d Cir. 1991), held that the "fundamental fairness" of the trial was undermined where the jury was misled into believing that defendant's good faith beliefs could negate the element of willfulness only if those beliefs were objectively reasonable. "The basic problem with the instruction given is that, on the issue of good faith, the jury was not instructed that it must consider whether defendant subjectively believed that he did not need to file income tax returns or pay taxes". *Id. Citing Cheek,* the *Pabisz* court concluded that the district court's failure to affirmatively instruct the jury that defendant's beliefs need not be objectively reasonable if they were actually held in good faith, was reversible error. *Id. See also Snyder v. United States,* 897 F. Supp. 241, 244 (D. Md. 1995) ("Thus, *Cheek* simply states that a good faith belief of legality, no matter how unreasonable, negates the statutory element of willfulness for tax evasion and failure to file a return, *and that a jury must be allowed to consider evidence of such a belief.*") (emphasis added).

The Seventh Circuit in *United States v. Havert*, 40 F.3d 197 (7th Cir. 1994), *cert denied*, 115 S. Ct. 1822 (1995), however, declined to adopt the reasoning of *United States v. Pabisz*, 936 F.2d 80, 83 (2d Cir. 1991), that the district court, in dealing with the good faith defense, must either instruct the jury to consider "whether [defendant] subjectively believed that he did not need to file income tax returns or pay taxes," or "that defendant's beliefs need not be objectively reasonable." In so holding, the *Havert* court stated, "*Cheek* does not mandate that the use of the word 'subjective' or words 'subjective standard' be stated in the charge to the jury. It does require the elimination of the words 'objectively reasonable' as applied to a willful violation of a known legal duty". *Havert*, 40 F.3d at 202. *See also United States v. Droge*, 961 F.2d 1030, 1038 (2d Cir. 1992) (jury instructions on "good faith" need not refer explicitly to the words "objective" and "subjective" intent); *United States v. Becker*, 965 F.2d 383, 388 (7th Cir. 1992) (jury instruction that "if the defendant actually believed that what he was doing was in accord with the tax statutes, he cannot be said to have had the criminal intent to willfully evade or defeat taxes or to willfully fail to file returns. This is so even if defendant's belief was not objectively reasonable as long as he held the belief in good faith" is an accurate summary of *Cheek* that appropriately focused the jury's attention on whether the defendant had a good faith belief he was acting lawful).

Unlike the instructions given in the present case, however, in both *Havert* and *Droge* the trial court instructions made it clear that defendant's good faith belief need not be objectively reasonable. *See Havert*, 40 F.3d at 202 (jury instructed that if the defendant in good faith believed that under the law he did not have any income tax obligation for a particular year, then any failure to pay income taxes for that year cannot be found to be willful, even if such belief *was incorrect*); *United States v. Droge*, 961 F.2d at 1038 (jury instructed that: "if you find that [defendant] sincerely and in good faith believed that the law was that he did not have to file a return because he was not required to by the Internal Revenue Code, then you cannot find that he acted willfully. Did he sincerely, honestly

believe what he said the law required, or did he in fact know that (sic) the law required and simply disagreed with it? It's for you to decide".) Indeed, in *Droge* the court pointed out:

> While the charge did not explicitly eschew an "objective" standard or expressly state that the jury had to employ a "subjective" standard in measuring the veracity of Droge's asserted beliefs, its emphasis on Droge's personal sincerity and good faith in those beliefs, and whether they were honestly held by Droge, adequately communicated the subjective approach that the jury was required to take.

Id.

The Third Circuit has held, however, that *no* additional instruction need be given to the jury in light of this Court's decision in *Cheek*. *See United States v. McGill*, 964 F.2d 222 (3d Cir. 1992). In *McGill*, the court concluded that *Cheek* only forbids an instruction that defendant's beliefs must be objectively reasonable, and does not place an affirmative duty on courts to instruct juries that defendant's belief need not be objectively reasonable. *Id.* at 238. Indeed, the court held that recitation of the customary definition of willfulness: the voluntary intentional violation of a known legal duty, without more, is permissible. *Id.* (rejecting defendant's argument that *Cheek* requires that a tax defendant is entitled to a particularized instruction concerning his actual knowledge of the tax laws). *See also United States v. Benson*, 67 F.3d 641, 650 (7th Cir. 1995), *reh'g denied*, 74 F.3d 152 (1996) (a precise definition of good faith highlighting subjectivity is not necessary to a willfulness instruction. District court did not plainly err that a good faith belief concerning the requirements of the tax laws may be subjective and need not be objectively reasonable. Although this is generally a correct statement of the law.) *(citing Cheek* and *United States v. Havert*, 40 F.3d 197 (7th Cir. 1994).

In rejecting Petitioner's argument that the district court erred in failing to advise the jury that Petitioner's belief, that he was doing all that was necessary to comply with the tax laws, need not be objectively reasonable, the Third Circuit Court of Appeals stated that Petitioner's argument introduces a distinction, "i.e., subjective belief as opposed to objectively reasonable belief that is not really at issue here." (3a). The panel found that the instructions in this case were different from *Cheek* in that they were based on Petitioner's state of mind and did not introduce the concept of Petitioner's reasonable beliefs. (4a). Petitioner respectfully submits, however, that this is a distinction without a difference. Indeed, what is reasonable to Petitioner by definition requires an inquiry into Petitioner's state of mind. Petitioner maintains that he believed in good faith that he was complying with his obligations under the tax code. If the jury agreed with him, yet believed that he was acting in an objectively unreasonable way, it was required to find him not guilty of the charges in the indictment. Further, as in *Cheek*, the jury in this case was clearly concerned about "whether the defendant honestly and reasonably believed that he was not required to pay the tax." (3a) *(citing Cheek)*. That this is so is clear from the jurors' question regarding reasonableness.

At the core of a defendant's guarantee to a fair trial is the trial court's obligation to assure that the jury's impartial deliberations upon the guilt of a criminal defendant are based solely upon the evidence in accordance with proper and adequate instructions. *See United Brotherhood of Carpenters and Joiners v. United States*, 330 U.S. 395, 408-409 (1946). Where jury instructions are ambiguous, an appeals court should inquire whether "there is a reasonable likelihood that the jury has applied the challenged instruction" in an improper manner. *Boyde v. California*, 494 U.S. 370, 380 (1990). Jury instructions must not be misleading and must contain an adequate statement of the law to guide the jury's determination. *United States v. Park*, 421 U.S. 658, 675 (1975). *See also Tigg Corporation v. Dow Corning Corporation*, 962 F.2d 1119 (3d Cir. 1992) (instructions taken as a whole must fairly apprise the jury of the issues and the applicable law). In addition, a defendant

is entitled to jury instructions presenting his theory of defense as long as the instructions are supported by the law and have a basis in the evidence presented to the jury. *United States v. Mason,* 902 F.2d 1434, 1438 (9th Cir. 1990).

Particularly under the facts of this case, where the reasonableness of Petitioner's conduct was severely drawn into question by the government, it was imperative for the trial court to clearly and unambiguously instruct the jury on the distinction between objective and subjective good faith. Its failure to provide that instruction constitutes reversible error and requires reversal of the judgment of conviction.

II. PETITIONER'S CONSTITUTIONAL RIGHTS TO DUE PROCESS WERE VIOLATED BY THE THIRD CIRCUIT'S AFFIRMANCE OF THE DISTRICT COURT'S DENIAL OF PETITIONER'S ACQUITTAL MOTION.

The due process clause of the constitution requires that the government prove beyond a reasonable doubt every element of the crime with which a defendant is charged. *In re Winship,* 397 U.S. 358, 364 (1970). In determining a motion for judgment of acquittal or for a new trial, the district court must decide whether there was "*substantial evidence*, viewed in the light most favorable to the government, to support the jury's finding of guilt beyond a reasonable doubt as to the elements of (each) crime charged." *United States v. Pecora,* 798 F.2d 614, 618 (3d Cir. 1986). *See also Government of the Virgin Islands v. Williams,* 739 F.2d 936, 940 (3d Cir. 1984).

Petitioner was charged with two counts of attempting to evade taxes, in violation of 26 U.S.C. § 7201. In order to obtain a conviction under 26 U.S.C. § 7201, the government must prove a willful violation, the existence of a tax deficiency, and an affirmative act of evasion or attempted evasion of the tax. *Sansone v. United States,* 380 U.S. 343, 351 (1965). It must be shown that the defendant had unreported income and that the income was taxable. *United States*

v. Chesson, 933 F.2d 298, 303-04 (5th Cir.), *cert. denied*, 112 S. Ct. 583 (1991). "Willfulness" is defined as the "voluntary, intentional violation of a known legal duty." *Cheek v. United States*, 498 U.S. 192 (1991). A "good faith misunderstanding of the law or a good faith belief that one is not violating the law negates willfulness, even if the claimed misunderstanding or belief is not objectively reasonable." *United States v. Bishop*, 412 U.S. 346 (1973). A defendant's good faith reliance on an expert tax preparer may be a defense to a tax evasion charge. *United States v. Meyer*, 808 F.2d 1304 (8th Cir. 1987).

Petitioner, who has an eighth grade education, should have been acquitted because the government failed to prove beyond a reasonable doubt, with substantial evidence, that he willfully evaded his tax obligations. As is set forth in detail in the statement of the case, Petitioner relied upon his accountants, who acknowledged that they were always given any information they requested of Petitioner, who further vouched for Petitioner's integrity, who admitted to not reviewing Petitioner's records on the yachts though they had been presented to them, who further admitted to over reporting Petitioner's income from the gas station by not deducting inter-account transfers, and who failed to ask Petitioner questions necessary to assess whether taxes were owed on the sale of the Brigantine property, though improvements to the property were of sufficient value to negate any tax obligation. The accountants' negligence was confirmed by Petitioner's expert, Robert Brennan, who testified that it did not matter whether the yachts were deemed to be short or long-term assets, because either way Petitioner would not have owed any additional taxes.

Because the government had not met its burden of proving all the elements of the crimes alleged beyond a reasonable doubt, the judgment of conviction must be reversed.

III. PETITIONER'S CONSTITUTIONAL RIGHT TO DUE PROCESS AND TO AN UNTAINTED GRAND JURY PROCESS WERE IRREPARABLY PREJUDICED BY THE PRESENTATION BEFORE THE GRAND JURY OF FALSE AND MISLEADING TESTIMONY BY INTERNAL REVENUE SPECIAL AGENT JACQUELINE ZISTERER.

A. Overview Of The Effect Of Agent Zisterer's Conduct On The Integrity Of The Grand Jury Proceedings.

Shortly before trial, Petitioner moved for the dismissal of the indictment on the grounds of grand jury misconduct. The misconduct came to light after Petitioner was supplied with the grand jury testimony of Internal Revenue Special Agent, Jacqueline Zisterer. Through testimony that was false and misleading, which wrongly informed the jury of not only the facts, but the law, and which contained improper comments upon Petitioner's alleged assertion of his Fifth Amendment rights, Zisterer tainted the functioning of the grand jury, infringing upon its mission to reach an independent conclusion on whether there was probable cause to return an indictment. These governmental encroachments were not only incompatible with the prosecutor's statutory obligations to prevent, among other things, perjurious testimony from coming before the grand jury, but such conduct subverted the institutional role of the grand jury. It is respectfully submitted that the trial judge erred in failing to dismiss the indictment and that Petitioner's constitutional rights, including his right to an unfettered grand jury determination, have been violated in the process.

B. The Historic And Constitutional Purposes Of The Grand Jury.

The Fifth Amendment to the United States Constitution guarantees to an accused the right to be indicted by a grand jury before being required to stand trial. U.S. Const. Amend. V. When the framers of the constitution included the Fifth Amendment in

the Bill of Rights "they were not engaging in a mere verbal exercise." *United States v. Estepa,* 471 F.2d 1132, 1136 (2d Cir. 1972). Rather, they recognized that the grand jury was essential to implementing "basic liberties". *United States v. Hogan,* 712 F.2d 757, 759 (2d Cir. 1983). The grand jury was devised to "provide a fair method for instituting criminal proceedings," *Costello v. United States,* 350 U.S. 359, 362 (1956), to serve "as a protector of citizens against arbitrary and oppressive governmental action," *United States v. Calandra,* 414 U.S. 338, 343 (1974), and to assure the "protect[ion] of citizens against unfounded criminal prosecutions." *Branzburg v. Hayes,* 408 U.S. 665, 686 (1972).

Despite the requirement that the grand jury act independently and that it serve as a buffer against oppressive governmental action, it has so often become prey to prosecutorial manipulation that the historic independence of the institution has been compromised. *United States v. Hogan,* 712 F.2d 757, 759 (2d Cir. 1983). This erosion of the independence of the grand jury stems from the active role that the prosecution plays in the proceedings. *Id.* It is the prosecutor who prepares the indictment, calls and examines witnesses, advises the grand jury as to the law, and is in attendance throughout the investigation. *Id.*

Though the prosecutor is actively involved in the proceedings of the grand jury, however, he or she does not have an absolute license to advocate a particular position. Rather, the prosecutor must act as "an administrator of justice". *United States v. Gold,* 470 F. Supp. 1336, 1346 (N.D. Ill. 1979). When prosecutors have infringed upon the independent functioning of the grand jury, courts have ordered indictments dismissed. *United States v. Hogan,* 712 F.2d 757, 761-62 (2d Cir. 1983); *United States v. Estepa,* 471 F.2d 1132 (2d Cir. 1972); *United States v. Roberts,* 481 F. Supp. 1385 (C.D. Calif. 1980); *United States v. Samango,* 607 F.2d 877, 883 (9th Cir. 1979); *United States v. DiGrazia,* 213 F. Supp. 232, 235 (N.D. Ill. 1963); *United States v. Serubo,* 604 F.2d 807, 818 (3rd Cir. 1979); *United States v. Gold,* 470 F. Supp. 1336, 1346 (N.D. Ill. 1979);

United States v. Treadway, 445 F. Supp. 959 (N.D. Tex. 1978); *United States v. DeMarco,* 550 F.2d 1224 (9th Cir. 1977); *United States v. Carcaise,* 442 F. Supp. 1209 (M.D. Fla. 1978); and *United States v. Morrison,* 518 F. Supp. 917 (S.D.N.Y. 1981).

After reviewing Petitioner's motion to dismiss the indictment, the district court concluded that, "Special Agent Zisterer made a number of erroneous or incomplete statements of a factual or legal nature to the grand jury." (DA-690a). The district court ultimately denied Petitioner's motion, however, notwithstanding its findings that:

> (1) Special Agent Zisterer's mistaken statement that former station manager Craig Matthews left that position in 1986 instead of 1984 was erroneous. [DA-691].
>
> (2) Zisterer's response to a question posed by a grand juror regarding the tax treatment of the gas station income was "elliptical" and "confusing, to say the least". [DA 691a].
>
> (3) "[R]eference to a $150,000 total diversion before the grand jury, while confusing and *imprecise*, did not constitute prosecutorial misconduct nor impermissibly influence the grand jury." [DA-691a].
>
> (4) *Agent Zisterer's explanations of when personal use transforms an investment property into a personal asset, "are incorrect statements of the law."* [DA-692].
>
> (5) "It was a mistake for Special Agent Zisterer to have referred *to defendant's Fifth Amendment rights . . .*" [DA-693].

> (6) "Taken in isolation, the quoted statements of Special Agent Zisterer are incomplete and thus, *inaccurate.*" [DA-694a].
>
> (7) Although, "[t]here was a degree of carelessness in the presentation to the grand jury in this case . . . instances of *incomplete information* or *loose language*. . . . It cannot be said that the errors . . . were so great as to impair the judgment of the grand jury." [DA-694-95].

Even the government conceded in its responding brief before Third Circuit Court of Appeals that "To be sure, the District Court found Zisterer's testimony to contain hearsay, to be contrary to the evidence adduced at trial, and to be inaccurate in some respects". (Gov't Br. at 17). The government wrongly maintained, however, that since there was no specific finding that Zisterer's testimony constituted perjury, there was no error. Petitioner strongly disagrees.

In *The Bank of Nova Scotia v. United States,* 487 U.S. 250 (1988), this Court set forth the standard to be applied in determining whether an indictment should be dismissed. The Court stated that dismissal was warranted only in those cases "in which the structural protections of the grand jury have been so compromised as to render the proceedings fundamentally unfair, allowing the presumption of prejudice." *Id.* at 257. Subsequently in *United States v. Soberon,* 929 F.2d 935 (3d Cir. 1991), the Third Circuit held that the presentation of perjurious testimony did not compromise the structural protections of the grand jury referred to in the *Nova Scotia* opinion. The court's holding in *Soberon,* however, has since been drawn into question by this Court's decision in *United States v. Williams,* 504 U.S. 36 (1992). There, although this Court held that the District Court did not have the power to dismiss an indictment for the prosecutor's failure to present exculpatory testimony, it premised its decision on the rationale that *Nova Scotia* permits exercise of the supervisory power of the Court to dismiss indictments to be used to remedy the violation of those "few, clear rules which

were carefully drafted and approved by this Court and by Congress to ensure the integrity of the grand jury's functions." *Id.* at 46. Among the rules and statutes specifically cited by the Court as being relevant to the grand jury's functioning were those relating to perjury. *Id.* at n. 6. *citing* 18 U.S.C. § 1623 (criminalizing false declarations before the grand jury) and § 1622 (criminalizing subornation of perjury).

This Court has thus recognized that specific standards of behavior for prosecutors, and specific statutes relating to perjury, are among the types of rules or laws that are intended to protect the integrity of the grand jury, and that *do* fall within the supervisory authority of the courts to dismiss indictments. Indeed, it is difficult to imagine how perjury could, under any circumstances, be tolerable, or not compromising of the grand jury's integrity. One of the central values of the justice system is truth. All witnesses, before they testify, must swear to tell the truth. Once the truth is disrespected, the integrity of the system is destroyed. It is for this reason, that convictions have been overturned where witnesses have been found to be lying.

In *Napue v. Illinois,* 360 U.S. 264 (1959), this Court held that due process is violated when the prosecutor obtains a conviction with the aid of false evidence which it knows to be false and allows to go uncorrected. *See also United States v. Barham,* 595 F.2d 231, 241 (5th Cir. 1979). It is immaterial whether or not the prosecution consciously solicited the false information. *Id.* at 241. And, similarly, it is immaterial whether the false testimony directly concerns an essential element of the government's proof or whether it bears only upon the credibility of the witness. *Id.* at 241-42.

This rule, that a conviction standing upon false testimony violates due process, was affirmed in *Giglio v. United States,* 405 U.S. 150 (1972), and again in *United States v. Bagley,* 473 U.S. 667 (1985), where the Court held that "a conviction obtained by the knowing use of perjured testimony must be set aside if there is any reasonable likelihood that the false testimony could have affected the jury's verdict. . . ." *Id.* at 679 n. 9. Due process is violated not

only when the prosecutor actively solicits false testimony, but also when he fails to correct false testimony. *Alcorta v. Texas,* 355 U.S. 28 (1957).

Courts have not hesitated to order new trials where false testimony has been used by the prosecution to obtain a conviction. *See, e.g., United States v. Bigeleisen,* 625 F.2d 203 (8th Cir. 1980) (false denial by witness of agreement to testify for prosecution); *United States v. Barham,* 595 F.2d 231 (5th Cir. 1979) (false denial by witness of promise of leniency); *United States v. SanFilippo,* 564 F.2d 176 (5th Cir. 1977) (false testimony regarding promise of immunity); *United States ex rel. Annunziato v. Manson,* 425 F. Supp. 1272 (D. Conn.), *aff'd,* 566 F.2d 410 (2d Cir. 1977) (false denial by witness of promises made in exchange for testimony); *Sanders v. United States,* 541 F.2d 190 (8th Cir. 1976) (false denial by witness of receipt of compensation). Application of the foregoing principals to these facts should have resulted in the dismissal of the indictment. Agent Zisterer had so contaminated and so manipulated the grand jury process through false statements and misleading omissions that the integrity of the proceedings was irreversibly compromised.

C. Agent Zisterer's False Testimony

One of the crucial issues the grand jury was asked to determine was whether Petitioner had properly characterized yachts he had sold as business assets. The grand jurors had specific concern about this issue. One juror was so concerned that he asked Zisterer a question. In response to the juror's question, the agent falsely told the entire grand jury that the moment a business asset is used for a personal purpose it becomes a personal asset. The following colloquy occurred in the grand jury room:

> A JUROR: You said he was hoping to make a gain on the sale of the yacht. Other than showing it to a number of potential buyers, how else would he have made a gain on that yacht?
>
> THE WITNESS: He wouldn't. When we

> purchase an asset, we would hope to sell it at a gain. Just by showing it to people does not turn that asset into a business asset. It has to be used strictly for business use. It just cannot be used for personal use. *The moment it is used for personal use, you can't take a deduction for loss.*

(DA-685) (emphasis supplied).

Zisterer's response to the grand juror's question was false. Treasury Regulation Section 183(b)(9) specifically declares that:

> It is not, however, necessary that an activity be engaged in with the exclusive intention of deriving a profit or with the intention of maximizing profits. . . . An activity will not be treated as not engaged in for profit merely because the taxpayer has purposes or motivations other than solely to make a profit. Also, *the fact that the taxpayer devised personal pleasure from engaging in the activity is not sufficient to cause the activity to be classified as not engaged in for profit if the activity is in fact engaged in for profit as evidenced by other factors whether or not listed in this paragraph.*

Id. (emphasis supplied).

Judge Debevoise recognized that Zisterer's testimony before the grand jury was inaccurate. (DA-692). He found, however, that the evidence presented by the government to the grand jury clearly established that it was the government's position that Petitioner had falsely informed his accountants that he had acquired his 46-foot yacht exclusively for investment purposes and had never used it for personal purposes. The judge also found that the agent, in responding to the question of another juror, had clarified her inaccurate

testimony, but that was not so. The colloquy relied upon by the judge was the following:

> A JUROR: You mentioned that you would have to — when he purchased the yachts, he indicated to the accountants that the use of the yachts were for business purposes.
>
> THE WITNESS: He said it was simply bought for business investments and not used for personal. It wasn't a personal use but for an investment.
>
> A JUROR: In I.R.S. laws, if you use the yacht at any time to talk about business, can you classify that as a business use?
>
> THE WITNESS: No. That doesn't make the yacht a business asset at that point, but it would allow you to take some deductions off your returns in connection with that business meeting. That wouldn't make the yacht itself a business asset, and ***the Internal Revenue Code states that anytime you use an asset for personal use, you cannot take a deduction for a loss on that.*** You can compare it real easy. *If you sell your automobile at a loss, you can't take a deduction on your tax return for that because you used it for personal use.*

(DA-693) (emphasis supplied).

If anything, the foregoing testimony compounds the prejudice suffered by Petitioner. Not only does the colloquy reflect continued concern on the part of the grand jury with the issue of when an asset is classified as business and when personal, but Zisterer, by stating again that an asset used for personal use cannot be deducted

as a loss and by further giving her automobile analogy, misled the grand jury for a second time. Her testimony caused the jury to believe that Petitioner, by using the yacht socially, had committed a crime when he treated the yacht as a capital asset for tax purposes.

Agent Zisterer's false testimony clearly had the capacity to cause Petitioner to be indicted by a grand jury that was concerned about the asset classification issue, yet was misinformed by one who professed under oath to know the law. The issue was particularly crucial because, during the year in question, Petitioner was developing his boat brokerage business and had been active in boating circles, including participation in social, but business-producing activities, during the start of his boating operation. Petitioner was clearly in the boating business, his assets were properly classified, and he had a right to engage in certain social activities to promote his business. Zisterer's testimony caused the grand jury to believe that once Petitioner used one of his assets for pleasure, any treatment of the asset as a business one for tax purposes was criminal.

D. More False Testimony Of Agent Zisterer

In addition to testifying falsely about the applicable law (and, as noted above, Judge Debevoise acknowledged that her testimony on this issue was inaccurate), Zisterer also misled the jury about the facts. She suggested to the grand jury that Petitioner gave his accountants one sheet of paper, on which he had written down the losses and profit he earned on the sale of the three yachts, and that he did this with the intention of misleading the accountants. Zisterer stated:

> Well, in respect to all the yachts reflected on the 1986 and 1987 returns, they (meaning the accountants) were provided with *one sheet of paper.* They were provided this piece of paper by Mr. Kennedy. It reflects the profit and the losses of all three yachts. *Those match the tax*

> *returns, so they simply took the losses and the one gain from this sheet of paper given to them by Mr. Kennedy.*

(DA-680, DA-694).

In fact, Zisterer's testimony was false, because she knew that the accountants, Moore and Kelly, had stated that Petitioner gave them three folders before his tax returns were prepared and those folders contained information that would have permitted the accountants to accurately prepare Petitioner's return. Not only did Zisterer attempt to mislead the jury by stating that Petitioner gave his accountants minimal and misleading information, but the tax returns prepared for Petitioner did not match, as Zisterer had claimed, what Petitioner put down on paper.

E. Still Further False Testimony from Agent Zisterer

Zisterer also falsely testified that Petitioner was "pocketing" money that did not go into either his business or personal accounts. The following exchange occurred between a grand juror and Zisterer:

> JUROR: In the pocketing of money that he put in his pocket (reference to Petitioner) do you have any papers or anything to prove that he pocketed — did you pick up any evidence to that?
>
> ZISTERER: The only evidence that I have in relation to what he put in his pocket is the testimony of the managers that delivered the cash to him at his personal residence that watched him do that. I do have the invoices which clearly substantiated the evidence that it wasn't reported on the tax returns. It didn't all appear to be going all into his personal bank

> accounts. When I added all these invoices up, they exceeded to about $150,000.00 to what was reported for automobile repairs on the tax returns. I was not able to trace all that going into the personal bank accounts. I don't know where the difference went, but it's an indication that it was put in his pocketed and used and spent.

(DA-690a to DA-691a).

Judge Debevoise referred to Zisterer's testimony on this issue as "elliptical" and "confusing, to say the least". (DA-691). Nevertheless he found that it was not prejudicial because there was evidence presented at trial of a diversion in excess of what the agent had stated. (DA-691a). In fact, Zisterer's testimony was false in several material respects. First, the government had paperwork in its possession that reflected inter-account transfers. When the government calculated Petitioner's gross receipts it failed to eliminate these transfers, which ended up in a double-counting of the receipts and in an overestimation of Petitioner's income. Further, merely because monies may have been deposited in a personal account does not mean that the monies were not first recorded in the business accounts. In fact, contrary to Zisterer's testimony, the government did have in its possession evidence that would have established that, if anything, Petitioner overstated his business receipts because his own accountants failed to eliminate inter-account transfers.

False testimony was also given by Zisterer on the issue of whether Petitioner had earned a commission on the sale of the 55-foot Uniflite yacht. Judge Debevoise referred to Zisterer's testimony on this issue as "conclusory", but he found that there was evidence to support her conclusion because the grand jury might have believed that Petitioner's profit on the sale was in fact a commission. (DA-693a). Although there was evidence that Petitioner had paid a commission in order to obtain a boat for Petitioner's buyer, Larry

Littman, there was no evidence that Petitioner was paid a commission. On the contrary, Larry Garr explicitly testified that Petitioner had *not* been paid a commission. This was an important issue because treatment of Petitioner's profit as a commission had different tax implications than if the profit derived from the sale of a capital asset.

Misleading testimony had also been offered about the Brigantine property. The government knew that the property, which Petitioner had sold, had been jointly owned by Petitioner and his mother and that his mother died two days before the deed was recorded, but after the deed had been prepared and signed. The jury was left with the inaccurate impression, however, that Petitioner was the sole owner of the property, had an obligation to pay taxes on it, and failed to do so.

F. Zisterer's Improper Comments On Petitioner's Alleged Assertion Of His Fifth Amendment Rights.

In addition to providing false and misleading testimony to the grand jury, Zisterer also improperly commented upon Petitioner's alleged assertion of his Fifth Amendment right to remain silent:

> THE WITNESS: Yes, I contacted Mr. Kennedy through correspondence. *He immediately obtained an attorney and took his Fifth Amendment right.* He didn't have to speak with me or provide me with anything. I contacted his attorney and asked him to provide me with substantiation of any nontaxable income he had.

(DA-684 to DA-685).

Petitioner maintained that it was not only improper for Zisterer to have made any mention of Petitioner having asserted his Fifth Amendment rights, but he maintained that the testimony itself was false. Through his counsel, Petitioner proffered to the Court that he

never asserted his Fifth Amendment privilege, either with respect to talking to the agent or to producing documents. Petitioner maintained that the agent's use of the word "immediate" was particularly prejudicial because it emphasized for the grand jurors Zisterer's suggestion that Petitioner had something to hide. The comment was not merely an infringement of Petitioner's Fifth Amendment rights, but was also an infringement of his right to counsel, inasmuch as Zisterer also commented on Petitioner having "immediately" obtained an attorney upon being contacted by the agent.

In this area, as in the others, Judge Debevoise found that Zisterer's comments were wrong, but not unduly prejudicial. The Judge acknowledged that Zisterer's testimony had the capacity to feed into a public perception that "a person who relies on the Fifth Amendment is likely to be guilty of some crime." (DA-693). Although the Judge found that Zisterer's comment was a "minimal reference" to Petitioner's Fifth Amendment rights, he found that the damage was ameliorated by Zisterer's further comment that Petitioner did not have an obligation to speak with her. That further comment, however, did not suffice to undo the damage already done. Zisterer had focused the grand jury's attention on Petitioner's immediate silence and retention of counsel, said nothing about his having a constitutional right to counsel, and left the jury with the clear and unmistakable impression that Petitioner had something to hide.

Recently, in *United States v. Breslin*, 916 F. Supp. 438 (E.D. Pa. 1996), the court considered a case strongly analogous to this one. There, the court dismissed an indictment because of prosecutorial misconduct. The court found that the prosecutor had mischaracterized the evidence, offered improper opinions about witnesses, and erroneously instructed the jury on the law, a fact that the court found was the "most disturbing" of all. The court was concerned with the cumulative effect of the prosecutor's conduct upon the grand jury.

The same concerns that motivated the court in *Breslin* to dismiss the indictment, should also have motivated Judge Debevoise to do so here. In this case, the government's principal witness testified falsely about fundamental principles of tax law, lied about crucial facts, and inappropriately commented upon Petitioner's assertion of his constitutional rights. Inasmuch as false legal principles and false facts, pivotal to the government's case, were communicated by the government to the grand jurors, the prejudice to Petitioner's fundamental rights is plain. The integrity of the grand jury was irreversibly compromised by the government's explicit violations of rules and laws intended to ensure the truth of information coming before the grand jury.

For all the foregoing reasons, the judgment of conviction against Petitioner must be reversed and the indictment must be dismissed.

CONCLUSION

For all the foregoing reasons, it is respectfully submitted that this Court should grant Petitioner's petition for issuance of a writ of certiorari.

Respectfully submitted:

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APPENDIX A — MEMORANDUM OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT FILED DECEMBER 4, 1996

NOT FOR PUBLICATION

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 94-5779

UNITED STATES OF AMERICA

v.

DENNIS F. KENNEDY

Dennis Kennedy,

Appellant

On Appeal from the United States District Court
for the District of New Jersey
(D.C. Crim. No. 93-00502)
District Judge: Honorable Dickinson R. Debevoise

Submitted under Third Circuit LAR 34.1(a)
November 25, 1996

BEFORE: GREENBERG, ALITO, and ROTH, *Circuit Judges*

(Filed: Dec. 4, 1996)

Appendix A

MEMORANDUM OPINION OF THE COURT

GREENBERG, *Circuit Judge.*

Appellant Dennis Kennedy appeals from a judgment of conviction and sentence entered on December 20, 1994, in this criminal tax case convicting him on two counts of tax evasion. The district court sentenced Kennedy to two concurrent four-month custodial terms followed by two concurrent three-year terms of supervised release. Kennedy raises the following three issues on the appeal: (1) the indictment against him should have been dismissed because Internal Revenue Special Agent Jacqueline Zisterer gave false and misleading testimony to the grand jury, which irreparably prejudiced Kennedy's rights; (2) the district court erred in denying Kennedy's motion to acquit him; and (3), on a plain error basis, the district court's "instructions failed to advise the jury that even if it believed that [Kennedy's] actions were objectively unreasonable, it still was required to acquit him if it found that he had acted in subjective good faith." We conclude that the first two issues which Kennedy raises lack merit and do not require discussion, and consequently, we address only the third issue.

Kennedy predicates his argument on *Cheek v. United States*, 498 U.S. 192, 111 S.Ct. 604 (1991). In *Cheek*, the Supreme Court made it clear that a defendant's good faith misunderstanding of the law or a good faith belief that he is not violating the law negates the willfulness element necessary to sustain a criminal tax conviction. Furthermore, the Court made it clear that a defendant's good faith belief does not have to be objectively reasonable. Of course, if the defendant's purported beliefs are not objectively reasonable, a jury might conclude that the defendant does not hold the beliefs in good faith. *Id.* at 203-04, 111 S.Ct. at 611-12.

Appendix A

Kennedy points out that the district court instructed the jury that if Kennedy "had a good faith misunderstanding of the law or believed in good faith that he had done all that the law required, you may not find that he acted willfully and you must acquit him." Kennedy then notes that the court instructed the jury that "[i]t is obviously impossible to ascertain or prove directly the operations of the defendant's mind; but a careful and intelligent consideration of the facts and the circumstances shown by the evidence in any case enables one to infer what another's intentions were in doing or not doing things. With the knowledge of definite acts, you may draw definite logical conclusions."

Kennedy does not quarrel with the foregoing instructions insofar as they go, but he contends that the instructions were not complete because the instructions permitted the jury to conclude that even though Kennedy had subjective good faith in dealing with his tax liability, he had acted objectively unreasonably and thus was guilty. In this regard, he points out that the court did not specifically instruct the jury that Kennedy's beliefs "need not be objectively reasonable for them to be in good faith." Br. at 31.

The problem with Kennedy's argument is that it introduces a distinction, *i.e.*, subjective belief as opposed to objectively reasonable belief, that is not really at issue here. In *Cheek*, the jury told the district court it was divided on whether the defendant honestly and "reasonably" believed that he was not required to pay the tax. The district court then instructed the jury that an "honest but unreasonable belief" that the defendant did not have to pay the tax was not a defense. The jury then convicted the defendant.

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The instructions here were different as they were based on Kennedy's state of mind and did not introduce the concept of Kennedy's reasonable beliefs into the jury's deliberations. Thus, the court told the jury that willfulness meant "the voluntary, intentional violation of a known legal duty." The court also explained that if Kennedy had "a good faith misunderstanding of the law or believed in good faith that he had done all that the law required," the jury had to find that he had not acted willfully and thus had to be acquitted. Furthermore, the district court told the jury that if "the government proves the defendant knew of his legal duty to file true and correct tax returns, and that he voluntarily and intentionally violated that duty, then you may find he acted willfully." These explanations of the law and the charge as a whole, which we have studied carefully, simply did not suggest to the jury that it should consider the reasonableness of Kennedy's beliefs. Rather, these explanations focused on Kennedy's state of mind without regard for the reasonableness of his beliefs. Thus, the charge was correct as it could not have misled the jury. Accordingly, the court in the charge did not commit error, let alone plain error.

In view of the aforesaid, we will affirm the judgment of conviction and sentence of December 20, 1994.

TO THE CLERK:

Please file the foregoing memorandum opinion.

s/ Morton I. Greenberg
Circuit Judge

DATED:

APPENDIX B — JUDGMENT OF THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT DATED DECEMBER 4, 1996

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 94-5779

UNITED STATES OF AMERICA

v.

DENNIS F. KENNEDY

Dennis Kennedy,

Appellant

On Appeal from the United States District Court
for the District of New Jersey
(D.C. Crim. No. 93-00502)

BEFORE: GREENBERG, ALITO, and ROTH, *Circuit Judges*

JUDGMENT

This cause came on to be considered on the record from the United States District Court for the District of New Jersey and was submitted under Third Circuit LAR 34.1(a) on November 25, 1996.

On consideration whereof, it is now here ADJUDGED and ORDERED by this court that the judgment of conviction and

sentence of the District Court entered December 20, 1994, be and is hereby affirmed.

ATTEST:

s/ P. Douglas Sisk
Clerk

DATED: Dec. 4, 1996

APPENDIX C — ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT DENYING PETITION FOR REHEARING DATED DECEMBER 30, 1996

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 94-5779

UNITED STATES OF AMERICA

v.

DENNIS F. KENNEDY

Dennis Kennedy,

Appellant

On Appeal from the United States District Court
for the District of New Jersey
(D.C. Crim. No. 93-00502)

SUR PETITION FOR REHEARING

BEFORE: SLOVITER, *Chief Judge,* and BECKER, STAPLETON, MANSMANN, GREENBERG, SCIRICA, COWEN, NYGAARD, ALITO, ROTH, LEWIS, and MCKEE, *Circuit Judges*

The petition for rehearing filed by the appellant, Dennis F. Kennedy, in the above captioned matter having been submitted to the judges who participated in the decision of this court and to all the other available circuit judges of the court in regular

active service, and no judge who concurred in the decision having asked for rehearing, and a majority of the circuit judges of the circuit in regular active service not having voted for rehearing by the court in banc, the petition for rehearing is denied.

BY THE COURT:

s/ Morton I. Greenberg
Circuit Judge

DATED: Dec. 30, 1996

APPENDIX D — OPINION OF THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY FILED SEPTEMBER 8, 1994

NOT FOR PUBLICATION

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

Hon. Dickinson R. Debevoise

Criminal Action No. 93-502

UNITED STATES OF AMERICA,

Plaintiff,

v.

DENNIS F. KENNEDY,

Defendant.

Appearances:

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Appendix D

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OPINION

DEBEVOISE, District Judge

A. *Background*

On October 14, 1993, a grand jury returned a two-count indictment against Dennis F. Kennedy charging him with tax evasion for the years 1986 and 1987.

With respect to the year 1986, the government charged that defendant's tax return was false and fraudulent in the following respects:

(a) On Schedule C of the tax return, defendant under reported the amount of gross receipts received by his Winslow Exxon gas station;

(b) On Schedule D of the tax return, defendant reported a $51,760 long-term capital gain on the sale of a 55-foot Ocean yacht when, in fact, the gain represented ordinary income;

(c) On Schedule D of the tax return, defendant reported a $40,862 capital loss on the sale of a 46-foot Ocean yacht, when, in fact, he had used the yacht primarily for personal and recreational purposes and was not entitled to claim the capital loss; and

(d) On Schedule D of the tax return, defendant failed to report a long-term capital gain from the sale of real estate located in Brigantine, New Jersey.

With respect to the year 1987, the government charged that defendant's tax return was false and fraudulent in the following respects:

(a) On Schedule C of the tax return, defendant under reported the amount of gross receipts received by Winslow Exxon gas station; and

(b) On Schedule D of the tax return, defendant reported a $69,422 capital loss on the sale of a 48-foot Uniflite yacht, when, in fact, he was not entitled to claim the capital loss.

The defendant denied these charges. At the trial, he contended with respect to the charge that he under reported gross receipts from the gas station (i) that there was, in fact, no under reporting in either 1986 or 1987 and (ii) that there was no intent to under report gross receipts in either year. With respect to each of the other false reporting or failure to report charges, defendant denied that there was intent on his part to erroneously report or to fail to report the item in question.

The jury found defendant guilty on both counts.

Immediately prior to trial, defendant moved to dismiss the indictment on the ground of prosecutorial misconduct before the grand jury. I reserved decision on the motion and proceeded with the trial. After the trial, defendant renewed his motion to dismiss. Briefs and exhibits have been submitted, and the parties have argued the motion.

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B. *The Alleged Misconduct*

Defendant charges that the grand jury testimony of Special Agent Jacqueline Zisterer was replete with inaccurate statements of fact, inaccurate hearsay and misstatements of the law and that these errors so tainted the government's presentation to the grand jury that its ability to exercise independent judgment was significantly impaired.

The government produced five witnesses before the grand jury — Lawrence Littman, who acquired the 55-foot Ocean yacht through defendant; Leonard Garr, who sold the 55-foot Ocean yacht to defendant; Robert Kelly and Kenneth Moore, who were the accountants who prepared defendant's 1986 and 1987 income tax returns and to whom, according to the government, defendant made false and misleading statements and failed to disclose critical information; and Special Agent Jacqueline Zisterer, the IRS employee charged with the responsibility of investigating and preparing this case.

Defendant has established that Special Agent Zisterer made a number of erroneous or incomplete statements of a factual or legal nature to the grand jury. I conclude, however, that in their total effect and in the context of the totality of Special Agent Zisterer's testimony and the testimony of the other grand jury witnesses, Special Agent Zisterer's lapses did not prejudice defendant or substantially influence the grand jury's decision to indict.

I shall discuss each of the deficiencies of which defendant complains.

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1. Defendant faults Special Agent Zisterer's testimony concerning diversion of funds from the service station. Initially he challenges her hearsay testimony recounting what two former managers of Winslow Exxon, defendant's former service station, told her about the diversion of cash receipts. It is not objectionable, of course, to present hearsay testimony to a grand jury. *United States v. Costello,* 350 U.S. 359, 363-64 (1956). Defendant contends that the particular hearsay testimony in this case was false.

Special Agent Zisterer testified before the grand jury that David Sagot told her that defendant instructed him on a regular basis to make deposits of gas station cash in his personal account. At trial, Sagot testified that he made three such deposits in 1986 and possibly an additional one in 1987, each for very small amounts. However, at the time when Special Agent Zisterer testified before the grand jury, she had Sagot's affidavit that 3-4 times a month defendant would ask him to deposit $200 to $300 of the day's cash receipts into his personal checking account. Thus, Special Agent Zisterer had a good faith reason to testify as she did about what Sagot had told her.

Special Agent Zisterer's mistaken statement that former station manager Craig Matthews left that position in 1986 instead of 1984 is a *de minimis* error.

During Special Agent Zisterer's testimony, a juror inquired:

> Q. In the pocketing of money that he put in his pocket (reference to Defendant) do you have any papers or anything to prove that he pocketed — did you pick up any evidence to that?

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Special Agent Zisterer replied:

> A. The only evidence that I have in relation to what he put in his pocket is the testimony of the managers that delivered the cash to him at his personal residence that watched him do that. I do have the invoices which clearly substantiated the evidence that it wasn't reported on the tax returns. It didn't all appear to be going all into his personal bank accounts. When I added all these invoices up, they exceeded to about $150,000.00 to what was reported for automobile repairs on the tax returns. I was not able to trace all that going into the personal bank accounts. I don't know where the difference went, but it's an indication that it was put in his pocket and used and spent.

This elliptical reply was confusing, to say the least. At the time the testimony was given, the government had evidence that defendant understated his auto repair receipts by approximately $87,000 during a thirteen-month period ending in October, 1984, although this evidence was not admitted at trial. Further, the government's evidence at the time of the grand jury hearing appeared to support substantially larger diversions in 1986 and 1987 than were proved at trial. In these circumstances, reference to a $150,000 total diversion before the grand jury, while confusing and imprecise, did not constitute prosecutorial misconduct nor impermissibly influence the grand jury.

2. Defendant asserts that the government deceived the grand jury by telling it that the diverted amounts were concealed by

defendant from his accountants when, in fact, defendant gave both his personal and business books and records to the accountants. I do not find an inconsistency between defendant providing the accountants with all his books and records and defendant concealing the diversions from his accountants. Perhaps careful accountants (which these clearly were not) would have detected diversions had they audited the books and records or examined them thoroughly. However, by failing to disclose diversions, defendant would have deceived the accountants even if he had provided books and records.

3. Defendant criticizes the government for failing to detect his accountants' error arising from their failure to reconcile all transfers between various bank accounts. Since the accountants determined gross income by adding up all the deposits into the bank accounts, transfers between bank accounts resulted in duplicated amounts and the overstatement rather than understatement of income.

While theoretically the government might have done what defendant's own accountants failed to do, at the time of the grand jury presentation, the government had substantial evidence from Sagot and Matthews which seemed to support a charge of diversion of cash proceeds from the service station to defendant's personal account. More was not required.

4. Defendant refers to inaccurate statements of the law which Special Agent Zisterer made during the course of her testimony. She stated concerning the sale of the yachts, "[t]he moment it is used for personal use, you can't take a deduction." She further stated, "and the Internal Revenue Code states that any time you use an asset for personal use, you cannot take a deduction for a loss on that."

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These statements are incorrect statements of the law. However, the evidence presented to the grand jury made it perfectly clear what the government's legal position was, namely, that defendant falsely informed his accountants (and, through them, the government) that he had acquired his 46-foot yacht exclusively for investment purposes and that he never used it for personal purposes:

> Q. What in the next item that's listed on that schedule?
>
> A. A 46-foot yacht. He's claiming a loss on the sale of the yacht.
>
> Q. What evidence did you come across which tells you that that is a false item?
>
> A. Basically, his return preparers told me they included this item on a Schedule D and included this on his return because Mr. Kennedy told them that he never used the yacht for personal use and it was simply purchased for investment, fixed up and sold. Throughout my entire investigation, I interviewed many people including Mr. Kennedy's brother, next door neighbor, employees, his business associates, his insurance man. I went to a Yacht Club where Mr. Kennedy was. Everyone told me that Mr. Kennedy used this yacht for personal use. They went on numerous trips with Mr. Kennedy, and to the best of all their knowledge, he used this solely for personal purposes.

> Q. Now, Did Mr. Kennedy have any real estate that was sold —
>
> A. Can I add one thing? The reason that this is not a deductible loss is because the Internal Revenue does not allow a deduction on our personal assets.

Tr. at 17-18.

At the end of her testimony, one of the grand jurors brought up the subject of the yachts again:

> A JUROR: You mentioned that you would have to — when he purchased the yachts, he indicated to the accountants that the use of the yachts were for business purposes.
>
> THE WITNESS: He said it was simply bought for business investments and not used for personal. It wasn't a personal use but for an investment.
>
> A JUROR: In I.R.S. laws, if you use the yacht at any time to talk about business, can you classify that as a business use?
>
> THE WITNESS: No. That doesn't make the yacht a business asset at that point, but it would allow you to take some deductions off your returns in connection with that business meeting. That wouldn't make the yacht itself a business asset, and the Internal Revenue Code states that anytime you use an asset for

> personal use, you cannot take a deduction for a loss on that. You can compare it real easy. If you sell your automobile at a loss, you can't take a deduction on your tax return for that because you used it for personal use.

Tr. at 37-38.

With that testimony in mind, it cannot be said that the grand jury was misled by her later observation that "[t]he moment it is used for personal use, you can't take a deduction for the loss" (Tr. at 39) and that "the Internal Revenue Code states that any time you use an asset for personal use, you cannot take a deduction for a loss on that." Tr. at 38.

5. Defendant notes Special Agent Zisterer's reference to his Fifth Amendment. Her testimony was as follows:

> A JUROR: Did you try to obtain any of the invoices from 1986?
>
> THE WITNESS: From Mr. Kennedy?
>
> A JUROR: Yes.
>
> THE WITNESS: Yes, I contacted Mr. Kennedy through correspondence. He immediately obtained an attorney and took his Fifth Amendment right. He didn't have to speak with me or provide me with anything. I contacted his attorney and asked him to provide me with substantiation of any nontaxable income he had.

Tr. at 38-39.

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It was a mistake for Special Agent Zisterer to have referred to defendant's Fifth Amendment rights, because in the minds of much of the public, a person who relies on the Fifth Amendment is likely to be guilty of some crime. However, it cannot be said that the minimal reference here rendered the proceedings fundamentally unfair, particularly when Special Agent Zisterer added after her reference to the Fifth Amendment the observation that "[defendant] didn't have to speak with me or provide me with anything. I contacted his attorney and asked him to provide me with substantiation of any nontaxable income he had."

6. Before the grand jury, Special Agent Zisterer made a conclusory statement that defendant earned a commission on the sale of the 55-foot Uniflite yacht to Larry Littman that would be reported ordinarily as ordinary income. Defendant contends that this characterization of the profit that defendant received on the sale of the yacht to Littman was misleading in light of statements which witnesses Garr and Littman had given to her and in light of their trial testimony, in which both men denied the existence of a commission arrangement. Defendant urges that the real question was whether the transaction resulted in a long-term or short-term capital gain, and that there would have been no tax consequences to defendant because of offsets from other capital gain transactions which were properly reported.

There was evidence, however, which supported Special Agent Zisterer's statement to the grand jury that the profit on the sale of the 55-foot Ocean yacht was a commission, received by defendant acting as buyer's agent for Littman. When Kennedy communicated with Comstock Boatworks, he was doing so in order to acquire the vessel for Littman. Two months after he signed the purchase agreement, defendant invoiced and delivered the yacht to Littman. Special Agent Zisterer's grand jury

characterization of the profit was reasonable, and it was the province of the trial jury to decide ultimately what the nature of the profit was.

7. Finally, defendant contends that the following statement of Special Agent Zisterer misled the grand jury:

> Well, in respect to all the yachts reflected on the 1986 and 1987 returns, they (meaning the accountants) were provided with one sheet of paper. They were provided this piece of paper by Mr. Kennedy. It reflects the profit and the losses of all three yachts. Those matched the tax returns, so they simply took the losses and the one gain from this sheet of paper given to them by Mr. Kennedy.

Defendant correctly notes that after he brought the sheet to his accountants, they informed him that they would need more information and that immediately thereafter he brought in the folders which contained all the information concerning purchase prices, summary of transactions, repair bills and sales contracts.

Special Agent Zisterer gave the testimony quoted above when summarizing the evidence of the falsely-reported yacht transactions for the benefit of a new grand juror who had not been present when the accountants had testified. Previously, both accountants (Moore and Kelly) had testified before the grand jury and told the grand jurors about the three folders of information and the summary information which defendant had provided on a sheet of paper. They further testified that they did not use the information in the folders to calculate gains or losses reported on the tax returns and instead relied on the summary information defendant provided them on the one sheet of paper.

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Taken in isolation, the quoted statement of Special Agent Zisterer is incomplete and, thus, inaccurate. However, in view of the accountants' testimony about all the documents which defendant provided to them, the quoted statement cannot have misled the grand jury in any way.

C. *Discussion*

"A district court may not dismiss an indictment for errors in grand jury proceedings unless such errors prejudiced the defendants." *Bank of Nova Scotia v. United States,* 487 U.S. 250, 254 (1988). An error prejudices the defendant if the violation substantially influenced the grand jury's decision to indict or "if there is grave doubt that the decision to indict was free from the substantial influence of such violations." *Id.* at 256. Absent a showing of prosecutorial misconduct, a defendant may not challenge an indictment on grounds that unreliable or incompetent evidence was presented to the grand jury. *Id.* at 261. "One challenging an indictment carries a difficult burden. He must demonstrate that the prosecutor engaged in flagrant misconduct that deceived the grand jury or significantly impaired its ability to exercise independent judgment." *United States v. Al Mudarris*, 695 F.2d 1182, 1185 (9th Cir. 1983).

There was a degree of carelessness in the presentation to the grand jury in this case, but there was nothing even approaching prosecutorial misconduct. The instances of incomplete information or loose language were rectified by other portions of the testimony before the grand jury. It cannot be said that the errors either singly or in the aggregate were so great as to impair the judgment of the grand jury. The case was tried before a jury; none of the objectionable grand jury testimony was presented to the trial jury; through unusually able counsel,

defendant availed himself of his right to present his contentions to the trial jury; the government's burden of proof at trial is a heavy one, compared to its burden before the grand jury; and the jury found defendant guilty of the charges contained in the indictment. This is confirmatory of my conclusion that the errors of the government during its grand jury presentation did not prejudice the defendant.

I shall file an order denying defendant's motion to dismiss the indictment.

s/ Dickinson R. Debevoise
DICKINSON R. DEBEVOISE, U.S.D.J.

DATED: September 8, 1994

APPENDIX E — ORDER OF THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY FILED SEPTEMBER 8, 1994

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

Hon. Dickinson R. Debevoise

Criminal Action No. 93-502

UNITED STATES OF AMERICA,

Plaintiff,

v.

DENNIS F. KENNEDY,

Defendant.

ORDER

For the reasons set forth in an opinion of even date,

IT IS THIS 8th day of September, 1994;

ORDERED that defendant's motion to dismiss the indictment is denied.

s/ Dickinson R. Debevoise
DICKINSON R. DEBEVOISE, U.S.D.J.

APPENDIX F — RELEVANT STATUTE AND CONSTITUTIONAL PROVISION INVOLVED

United States Constitution, Amendment V:

> No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury. . . .

26 U.S.C. § 7201:

> Any person who willfully attempts in any manner to evade or defeat any tax imposed by this title or the payment thereof shall, in addition to other penalties provided by law, be guilty of a felony and, upon conviction thereof, shall be fined not more than $100,000 ($500,000 in the case of a corporation), or imprisoned not more than 5 years, or both, together with the costs of prosecution.